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IN THE

Supreme Court of the United States

October Term, 1940.

No. 817

THE ROYAL INDEMNITY COMPANY,
Petitioner,

vs.

THE UNITED STATES OF AMERICA.

Petition for a Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

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INDEX.

	PAGE
Origin of the Case	1
Jurisdiction	1
Questions Presented	2, 3
Statutes Involved	3, 4
Statement	4, 5
Specification of Errors	5, 6
Reasons for Granting the Writ	6, 8
Brief	9
Point I	9–12
Point II	12, 13
Point III	13

TABLE OF CASES CITED.

Board of Education of Boyd County v. Trustees of Buena Vista School, 256 Ky. 432 11

Brewerton v. United States, 9 F. Supp. 503 ..... 6, 10, 11

City of Wilburton v. King, Atty. Gen., 18, P. 2d 1075-1077 11

Cornell v. Harris, 88 P. 2d 498 11

Guillot v. State Highway Commission of Montana, 56 P. 2d 1072 11

Haynes v. Butler, 30 Ark. 69 10

Hinemann Chemical Co., et al. v. United States, 92 F. (2d) 302-304 ..... 6, 10, 11

In re Farell, 36 Mont. 257, 262 10

PAGE

Jourolmon v. Ewing, 80 F. 604, 607, 608 ..... 7, 13

Kasik v. Janssen, 158 Wisc. 606, 609, 610 11

Mason v. Walkovich, 150 F. 699, 700, 706 ..... 7, 13
Mayor, etc., of New York v. Sands, 105 N. Y. 210, 218 11
Mitchell v. Kelsey, F. Cas. No. 9, 664 ..... 7, 13

O'Neil v. Goldenetz, 85 P. 2d 705 11
Opinion of Atty. Gen., Vol. 4, p. 312, Vol. 7, p. 62, Vol. 33, p. 441 9

Redfield v. Bartels, 139 U. S. 694 ..... 7, 13
Redfield Executrix v. Ystalyfera Iron Co., 110 U. S. 174, 176 ..... 7, 13
Reliance Mfg. Co. v. Board of Prison Commissioners, 161 Ky. 135, 142 10
Rives, et al. v. U. S., 28 Ct. Cls. 249, 251 10

State v. Burleigh County, 19 N. D. 819, 834, 835 .. 10
State v. Great Northern R. Co., 68 Wash. 257, 262.. 11
State v. Hackmann, 276 Mo. 110, 116 10
State v. Hildebrant, 93 Oh. 1, 2, 11, 12 11
State v. Illinois Cent. R. Co., 92 N. E. 814, 815, 832 10
State on inf., McKittrick v. Wymore, 132 S. W. 2d
State v. Rose, 140 Wis. 360 11
Stewart v. Schell, 31 F. 65, 66 ..... 7, 13
State, ex rel., Taylor v. Superior Court of Kings County, 98 P. 2d 985 11
State v. Younkin, 108 Kansas 634, 638 10
979 11

U. S. v. Alexander, 110 U. S. 325 11
United States v. Sanborn, 135 U. S. 271, 281, 282 .. 7, 13
U. S. Treasury Decisions G. C. M., 8980, Cum. Bull., X-1, page 256 9
United States v. Wagner, 93 F. (2d) 77, 79 ..... 7, 12
United States v. Walper, 86 F. (2d) 715, 717 7

STATUTES CITED.

	PAGE
Section 3 (b) Act of February 13, 1925	1
Act of May 22, 1939	2, 6
Section 3183, R. S.	2, 6, 9
Section 1541 (a) 26 U. S. C.	2, 4, 9
Section 1549, 26 U. S. C.	2, 4, 9
Section 1733 (a) (b) (c) (d) p. 1206, Title 26 Code Laws of U. S. 1934 Ed.	12
Section 370, New York Gen. Bus. Law	2, 12
Section 262, Title 28, Code Laws U. S., 1934 Ed.	12
Section 5, Title 6, Code Laws U. S., 1934 Ed.	12
Section 1432 (a), Title 26, Code Laws, U. S., 1934 Ed.	12
Section 474, Title 26, Code Laws U. S., 1934 Ed.	12
Section 347, Title 28, Code Laws U. S., 1934 Ed.	2

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OCTOBER TERM, 1940.

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THE ROYAL INDEMNITY COMPANY,
Petitioner,

vs.

THE UNITED STATES OF AMERICA.

Petition for a Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

The petitioner, The Royal Indemnity Company, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above entitled cause, December 26, 1940. Opinion filed December 9, 1940.

Opinion Below.

The opinion of the Circuit Court of Appeals is reported in 116 F. (2d) 247.

The opinion of the District Court is in the record (R., pp. 22-24).

Jurisdiction.

The opinion of the Circuit Court of Appeals was filed December 9, 1940 (R., pp. 30-34) and judgment entered December 26, 1940 (R., p. 35). The jurisdiction of the Court is invoked under Section 3 (b) of the Act of February 13,

1925, as amended by the Act of May 22, 1939. Section 347, Title 28, Code of Laws, U. S. 1934 Ed.

Questions Presented.

1. Whether the Collector of Internal Revenue is vested with implied power derived from his expressed power to collect taxes as provided by Section 3183 R. S. and Section 1541 (a) 26 U. S. C. and to give receipts for all taxes collected as provided by Section 1549, 26 U. S. C., to accept in his name as such collector a surety bond and stay the collection of taxes pending a decision on a claim in abatement and after such decision and demand by the collector for payment, and payment by the surety which payment was accepted by the collector as full satisfaction of liability of the bond, discharges the surety from all liability thereunder and cancel and return the bond to it.

2. Whether under the terms of a surety bond (the bond involved herein) given by a taxpayer to a collector of Internal Revenue to stay collection of taxes pending a decision of a claim in abatement, which bond makes no reference to a state law[1] providing interest at the legal rate of 6%, is the surety liable for such interest.

3. Whether a surety on a bond given by a taxpayer to a collector of Internal Revenue to stay collection of taxes pending a decision of a claim in abatement is liable to the United States for a legal rate of interest at 6% provided by New York State Law[2], or any other law and the United

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1 and 2. Section 370. New York Gen. Bus. Law.

"The rate of interest upon the loan or forbearance of any money, goods, or things, in action, except as otherwise provided by law, shall be six dollars upon one hundred dollars, for one year; and at that rate for a greater or less sum, or for a longer or shorter time."

The New York Courts in construing this statute have held: that interest is only allowed when there is a contract express or implied to pay interest, or as damages for the non-payment of money due. *Matter of New York, etc., Bridge*, 137 N. Y. 95. Claims unliquidated do carry interest. *Sloan v. Baird*, 162 N. Y. 327. Interest may be waived by acceptance of principal; *McCreery v. Day*, 119 N. Y. 1; Cutter 1. New York, 92 N. Y. 166.

States being guilty of laches without just excuse in not instituting and prosecuting suit for more than nine years after the accrual of the right.

Statutes and Regulations Involved.

So far as petitioner has been able to ascertain there is no Internal Revenue Law expressly empowering the collector to accept a surety bond from a taxpayer[3], to stay the collection of taxes. There is no Internal Revenue Law expressly empowering the collector, the Commissioner of Internal Revenue, or any other officer of the government to cancel such bonds and discharge sureties from liability, even where the provisions of the bond have been fully complied with[4]. Necessarily, therefore, their power to do so must be implied.

The implied power of the collector to discharge sureties from liability of such bonds is derived from the following statutes:

Collection Authority.

(a) In general; within district.

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3 and 4. The Treasury Department has ruled that neither the Collector or Commissioner of Internal Revenue are vested with express statutory power to rescind and cancel surety bonds. The ruling is as follows: "This office is of the opinion that, even where payments by a principal or a surety satisfy the liability under a bond there is no provision of law authorizing the Commissioner or Collector to issue to a principal or surety a certificate of release therefrom and that accordingly, there is no authority for the execution of the form submitted by the surety in the instant case purporting to release the surety from further liability under the bond furnished by it. The bond, therefore, should be retained in the files of the Bureau. However, if the Bureau is satisfied that the taxpayer or surety have paid the amounts of the tax and interest covered by the bond in accordance with the terms of the extension granted the collector or the Bureau may so advise the surety". G. C. M., 8980, Cum. Bull. X-1, page 256. See also, 4 opinion. Atty. Gen., 312, 7, opinion, Atty. Gen. 62, 33, opinion. Atty. Gen. 441. Since it appears that the Collector and Commissioner lack express power to cancel and return the bond, and since it is ruled by the Bureau they may advise the principal and surety that the tax liability has been satisfied. It is reasonable and logical they are vested with implied power to cancel and return the bond.

"It shall be the duty of the collectors or their deputies, in their respective districts and they are authorized to collect all the taxes imposed by law, however the same may be designated." See 1541 (a) 26 U. S. C.

(b) Receipts for taxes; in general.

"Every collector and deputy collector shall give receipts for all sums collected by him. * * * " Section 1549, 26 U. S. C.

Statement.

The facts in the record and as stated by the Circuit Court of Appeals may be summarized as follows:

This is an action by the United States against the surety on a bond given by a taxpayer as principal to the collector of Internal Revenue for the Second Collection District of New York (R., pp. 2-10).

The bond dated May 22, 1922, in the sum of $38,000.00 was given to obtain a stay of collection of an income tax deficiency for the year 1917, as to which the taxpayer had filed a claim in abatement with the Commissioner of Internal Revenue. The bond was conditioned on payment of so much of the deficiency as should not be abated with interest (R., pp. 11-12, Ex. B, p. 16).

Under date of February 18, 1925, the Commissioner of Internal Revenue allowed the claim in abatement in part and rejected it in the amount of $8,223.67. Demand was made by the Collector on the taxpayer for payment and upon his default, on the surety (R., p. 12).

On December 17, 1926, the surety paid to the collector by draft the sum of $8,223.67 in full settlement and for discharge of liability of the bond and the Collector so accepted the same. The draft bore on its face a notation that it was in full settlement of the taxes for 1917, and

all liability under the bond. Thereafter and on December 20, 1926, the Collector cancelled the bond and transmitted it to the surety with a letter stating: "All liability under this bond is hereby terminated". The surety then closed the case in its files (R., pp. 13-14, Ex. C, p. 17).

Thereafter and on September 23, 1932, the then Collector of Internal Revenue made demand upon the surety for the payment of an additional sum as interest. The surety refused to pay the same, or any other amount relying upon the payment and settlement of December 17, 1926, and the cancellation and return of the bond to it of December 20, 1926 (R., p. 14).

Thereafter and on April 27, 1935, this action was commenced, and upon the complaint, answer and agreed statement of facts each party moved for summary judgment (R., pp. 2-10, 19-21).

The District Court entered judgment for the plaintiff in the sum of $4,169.07 and denied recovery for legal rate of interest at 6% provided by New York State Law (R., pp. 22-26).

Both parties appealed to the Circuit Court of Appeals, the surety from the judgment entered against it and the United States from the denial of the legal rate of interest at 6% as provided by New York State Law (R., pp. 26-27).

The Circuit Court on defendant's appeal affirmed the judgment of the District Court and on plaintiff's appeal modified the judgment to include interest at the rate of 6% per annum from December 17, 1926 (R., pp. 30-34).

Specification of Errors to Be Urged.

The Circuit Court of Appeals Erred:

1. In holding that the Collector of Internal Revenue lacked implied power to cancel and discharge the surety from liability under the provisions of the surety bond

and in affirming the judgment of the District Court for $4,167.07.

2. In holding, that under the terms of the surety bond the surety was liable for the legal rate of interest at 6% provided by New York State Law from December 17, 1926.

3. In holding, that notwithstanding the laches of the United States of approximately nine years in the institution and prosecution of its claim; that the United States is entitled to recover interest at the rate of 6% as provided by New York State Law from December 17, 1926.

4. In failing to enter judgment for petitioner and dismissing the cause of action of the United States.

Reasons for Granting the Writ.

The decision of the Circuit Court that the Collector of Internal Revenue lacked implied power to cancel the bond and discharge the surety from liability thereunder is in direct conflict with the decision of the Circuit Court of Appeals for the Third Circuit in *Hinemann Chemical Co., et al.* v. *United States,* 92 F. (2d) 302-304. The Court there held that under Section 3183, R. S., 26 U. S. C., Section 1541 (a), which expressly authorized the Collector to collect all taxes, that he was vested with implied power to cancel such bonds and terminate liability thereunder.

The decision of the Circuit Court is also in direct conflict with the decision of the United States Court of Claims in *Brewerton* v. *United States,* 9 F. Supp. 503. The Court there held that the Collector of Internal Revenue was not only the proper party to advise the surety of the status of liability for which the bond was given, but was also the proper party to determine when the bond could be released and authorize its release.

The decision of the Circuit Court that the United States is entitled to recover interest at 6% provided by New York State Law, Section 370, New York Gen. Bus. Law, *supra*, is in direct conflict with the decision in *United States* v. *Wagner*, 93 F. (2d) 77, 79.

The decision of the Circuit Court that the United States is entitled to recover interest at 6% provided by New York State Law, notwithstanding its laches of approximately nine years in instituting and prosecuting the suit is in direct conflict with the decisions of this Court in *Redfield Executrix* v. *Ystalyfera Iron Co.*, 110 U. S. 174, 176; *United States* v. *Sanborn*, 135 U. S. 271, 281, 282, *Redfield* v. *Bartels*, 139 U. S. 694, and the decisions of the lower Federal Courts as follows: *Mason* v. *Walkowich*, 150 F. 699, 700, 706; *Jourolmon* v. *Ewing*, 80 F. 604, 607, 608; *Stewart* v. *Schell*, 31 F. 65, 66; *Mitchell* v. *Kelsey*, F. Cas. No. 9, 664. In the *Ystalyfera* case, the Court there held when interest is recoverable not as a part of the contract but by way of damages, if plaintiff has been guilty of laches in unreasonably delaying the prosecution of its claim interest may be properly withheld. In the *Sanborn* case, the Court held the same rule applied to the government.

The questions presented are of considerable importance to taxpayers, sureties and the government. Collectors in the collection of the taxes negotiate directly with taxpayers and sureties with reference to amounts due, stay of collection and surety bonds, and as a whole are the only official that do.

Although there is no express statutory authority empowering collectors to accept surety bonds the practice has long been permitted and recognized[1]. He is the sole negotiator in reference to them and his acts, negotiations and discharge of liability have been, and are relied on by

1. *United States* v. *Wolper*, 86 F. (2d) 715, 717.

taxpayers and sureties as valid and binding and is a very important matter in the collection of the revenue and the uncertainty with reference to his authority especially with reference to his authority to accept and terminate liability of surety bonds tends to confusion and taxpayers and sureties cannot safely rely upon negotiations with collectors. It is clearly apparent therefore, that the problem here presented will constantly recur unless finally settled by the Court and the questions are of general importance.

Therefore, it is repectfully submitted that this petition for a writ of certiorari should be granted.

March, 1941.

Respectfully submitted,

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BRIEF.

Statement of Fact.

The facts are stated in the petition, pages 3, 4.

Argument.

POINT I.

The Collector of Internal Revenue was vested with implied power to cancel the bond and release the surety from further liability. This implied power is derived from his expressed and exclusive power over the collection of taxes vested in him by Section 3183, R. S., 26 U. S. C., Section 1541 (a) and Section 1549, *supra*.

Expressed power is not granted to either the Commissioner or Collector of Internal Revenue to cancel and release liability and return surety bonds to the surety. This the Treasury Department has so ruled. G. C. M., 8980, Cum. Bull., X-1, page 256. See, also, opinions of Attorney General, Vol. 4, page 312, Vol. 7, page 62, Vol. 33, page 441, *supra*. In the Treasury ruling, *supra*, it was said: "However, if the bureau is satisfied that the taxpayer and/or the surety in this case have paid the amounts of the tax and interest and/or penalty covered by the bond in accordance with the terms of the extension granted the Collector or bureau, may so advise the surety". By the foregoing, it is clear that the Treasury Department recognizes that the bureau and Collector are vested with implied power to notify the surety that the bond has been satisfied, this is equivalent to a release or discharge of liability of the bond and the return of it to the surety.

The bond must be filed with the Collector who, alone, is vested with exclusive express power over the collection of the taxes and thereby he is vested with all other power (im-

plied power) necessary within his discretion for the proper performance of his duties and one of such implied powers, authorized him to cancel and return the bond to the surety. The taxpayer is not alone interested. The surety is vitally concerned. The Collector is the only officer of the government vested with exclusive power over the collection of the taxes. The bond is filed with him and all negotiations with reference to the taxes and the bond are with the Collector and with no other, and the surety is justified in relying on the action of the Collector in cancelling and returning the bond to it, as being valid under the Collector's implied power.

The following authorities directly support the aforegoing contention: *Hinemann Chemical Co.* v. *U. S.*, 92 F. (2d) 302, 303, 304; *Brewerton* v. *U. S.*, 9 F. Supp. 503, 505, 507, *supra*; *Rives, et al.* v. *U. S.*, 28 Ct. Cls. 249, 251.

The law is well settled that a governmental officer, which should include Collectors of Internal Revenue, and which we think does, in addition to the powers expresaly conferred on them have by implication such powers as are necessary for the due and efficient exercise of the powers expressly granted. Respectfully, we contend that these legal principles apply to the fact situation of the case at Bar and as illustrating the application of the legal principle of implied power vested in the Collector to cancel and return the bond to the surety, we cite the following authorities:

Haynes v. *Butler*, 30 Ark. 69;
Reliance Mfg. Co. v. *Board of Prison Commissioners*, 161 Ky. 135, 142;
State v. *Illinois Cent. R. Co.*, 92 N. E. 814, 815, 832;
State v. *Younkin*, 108 Kansas 634, 638;
State v. *Hackmann*, 276 Mo. 110, 116;
In re Farell, 36 Mont. 254, 262;
State v. *Burleigh County*, 19 N. D. 819, 834, 835;

State v. *Hildebrant*, 93 Oh. 1, 2, 11, 12;
State v. *Great Northern R. Co.*, 68 Wash. 257, 262;
Kasik v. *Janssen*, 158 Wisc. 606, 609, 610;
State v. *Rose*, 140 Wis. 360;
City of Wilburton v. *King, Atty. Gen.*, 18, P. 2d 1075-1077;
Mayor, etc., of New York v. *Sands*, 105 N. Y. 210, 218;
State on inf., McKittrick v. *Wymore*, 132 S. W. 2d 979;
State, ex rel., Taylor v. *Superior Court of Kings County*, 98 P. 2d 985;
O'Neil v. *Goldenetz*, 85 P. 2d 705;
Cornell v. *Harris*, 88 P. 2d 498;
Guillot v. *State Highway Commission of Montana*, 56 P. 2d 1072;
Board of Education of Boyd County v. *Trustees of Buena Vista School*, 256 Ky. 432.

The Circuit Court of Appeals in its decision fails to consider that the decision in the *Hinemann Chemical Co.* case, and the decision of the Court of Claims in the *Brewerton* case, *supra*, were mainly based on the implied power of the Collector derived from the express power, vested in him over the collection of the taxes and not wholly and alone, based on the decision in *U. S.* v. *Alexander*, 110 U. S. 325. The question of implied power was not involved in the *Alexander* case. The main question involved was the power of the Secretary of the Treasury to reopen the case, once closed. Therefore, we respectfully disagree with the Circuit Court of Appeals, that there was a misapplication of the *Alexander* case to the decision in the *Hinemann Chemical Co.* and *Brewerton* cases.

The cancellation and return of the bond to the surety does not discharge the taxpayer from liability nor the Collector for he has given bond to protect the govern-

ment. Sec. 1733 (a), (b), (c), (d), P. 1206, Title 26, Code of Laws, United States 1934 Edition. Therefore, the government has a right of action against the taxpayer and the Collector, unless the action is barred by the Statute of Limitations.

There is no Statute of Limitation applying to this action, in so far as the petitioner has been able to ascertain. However, there are Statutes of Limitations applying to taxes and interest involved, and other actions both for and against the government[1], and following the policy of the Statute of Limitations, there should be such limitation of the action in the case at Bar and the government's right to recover, should be barred by the Statute of Limitations. The equities of the case at Bar should be considered in the light of all these circumstances.

POINT II.

The bond, the basis of this action, makes no reference either expressly or by inference to interest provided by Section 370, New York Gen. Bus. Law (see bond, Exhibit B, R., p. 16). Such interest, therefore, was not in contemplation of the parties to the contract of surety and, therefore, cannot be said to be a part of the contract. Only interest provided by the Internal Revenue Law may be considered as in contemplation of the parties and thereby an element of the contract. *United States* v. *Wagner*, 93 F. (2d) 77, 79. It is clear, therefore, if the surety under any circumstances is liable for the legal rate of

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1. Limitation to bring actions against the United States in U. S. Courts and Court of Claims is generally six years. Section 41 (20) (Judicial Code, Section 24 Amended); Section 262, Title 28, Code Laws, U. S. 1934 Ed.

Limitation of actions against sureties in certain cases is five years. Section 5, Title 6, Code Laws, U. S. 1934 Ed.

Limitation actions, U. S. Court of Claims, generally six years. Section 262, Title 28, Code of Laws, U. S. 1934 Ed.

Limitation on assessment of Internal Revenue tax, four years. Proceedings in Court to collect tax, five years. Section 1432 (a), Title 26, Code of Laws, U. S. 1934 Ed.

Limitation on estate tax, three years, suits in Court, three years. Section 474, Title 26, Code of Laws, U. S. 1934.

interest provided by New York State Law, it is by way of damages and which will be fully considered in the next point.

POINT III.

The undisputed facts of the case at Bar disclose that the government is guilty of gross laches in asserting its claim and in instituting and prosecuting its suit. It was approximately eighteen years after the tax was due, and nine years after payment by the surety, the cancellation and return of the bond to it, that the government instituted this action to enforce its claim (see dates of Complaint, R., 7, cancellation and return of the bond, R., 10, 11, 13). The law is well settled that where such interest is claimed as damages and not as a part of the contract, interest will not be allowed if the creditor is guilty of laches. *U. S.* v. *Sanborn*, 135 U. S. 271, 281, 282; *Redfield* v. *Ystalyfera Iron Co.*, 110 U. S. 174; *Redfield* v. *Bartels*, 139 U. S. 694; *Mason* v. *Walkowich*, 150 F. 699, 700, 706; *Jouralmon* v. *Ewing*, 80 F. 604, 607, 608; *Stewart* v. *Schell*, 31 F. 65, 66; *Mitchell* v. *Kelsey*, F. Cas. No. 9, 664, Section 32, page 190, Vol. 33, C. J. The same rule has been held by this Court to apply to the government. *U. S.* v. *Sanborn*, 135 U. S. 271, 281, 282, *supra*.

The petitioner, Royal Indemnity Co., respectfully urges that the writ of certiorari should be granted and the case considered by this honorable Court and the opinion and judgment of the Circuit Court of Appeals should be reversed and the cause of action dismissed.

March, 1941.

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